Chapter: 5

PATTERN OF FINANCING THE SAMPLE URBAN UNORGANISED ENTERPRISES

5.1: INTRODUCTION:

It is already discussed in the previous chapters that inadequacy of capital or lack of access to credit is one of the problems experienced by a larger percentage of unorganised enterprises. One segment of literature also states that the unorganised enterprises do not have access to credit from Formal Financial Institutions (FFIs) (NCEUS, 2007; Fazari, 2014; Bhavani and Bhanumurthy, 2015). As a result, own savings and credit from the informal sources plays an important role in financing their business. Here, queries arise regarding the pattern of financing their business by the unorganised enterprises under study. One segment of literature, specially in the agricultural financing states that the pattern of financing capital expenditure is different from that of financing working capital expenditure (Khaund, 2002). Farazi (2014) also found that the share of bank loan in the total amount of capital investment is higher compared to that in working capital expenditure. So, these two aspects are to be discussed separately. Sometimes, an unorganised entrepreneur may also borrow for expenditure on things other than their business. Queries also arise regarding the pattern of such loan; which is also discussed in this chapter.

This chapter consists of five sections. The second section discusses the pattern of financing capital investment made by the unorganised enterprises during last five years. The third section is about the pattern of financing working capital expenditure of the unorganised enterprises during last one year. The pattern of loans taken by the unorganised enterprises to spend on things other than business is explained in the
fourth section. The fifth and final section summaries the discussion and concludes with concluding remark.

5.2: PATTERN OF FINANCING CAPITAL INVESTMENT:

Investment in capital goods is important for any enterprise. Capital investment is the part of investment either to start a new business or for the large scale expansion of the existing ones. The production and productivity of any enterprise depends on the amount of capital invested in that activity. The need for capital investment is not equal for all the sectors of the economy. Moreover, it is difficult to have information regarding the capital investment made by the enterprises in a distant past. So, data was collected from the sample enterprises about the capital investment they made during last five years. In Guwahati, out of the 159 enterprises surveyed, 87 made capital investment during last five years. In Silchar, out of 46 enterprises surveyed 29 made capital investment during last five years. Among the entrepreneurs which made capital investment during last five years, 27 in Guwahati and 14 in Silchar made it entirely from own fund; while the rest took at least some amount of loan from different sources for capital investment. While 43.9% of the enterprises did not make any capital investment during last five years; 20% of the entrepreneurs made entire capital investment from their own fund. Thus, 63.9% of the entrepreneurs did not take any loan to finance their capital investments and the rest took loan to finance at least certain percentage of their capital investment. Only 9.27% of the enterprises financed their entire capital investment through borrowing. More than 80% of the entrepreneurs did not take any loan from the FFIs for capital investment; while the rest borrowed at least certain percentage of their capital investment from the FFIs. Thus, 16.6% of the entrepreneurs took loan only from non institutional sources to finance their capital investment. Only 7.32% of enterprises financed their entire capital investment through borrowing from FFIs.
A particular enterprise may take loan from different sources to finance their business. Here, queries arise regarding the percentage share of different sources in the total amount of capital investment made by the unorganised enterprises. The pattern of capital investment made by different categories of unorganised enterprises is explained with the help of figure: 5.1.

**Figure: 5.1: Pattern of Capital Investment made by Different Categories of Enterprises during Last Five Years**

Source: Field Survey, June-September, 2015

Figure: 5.2 shows that around 49% of the capital investment expenditure made by the unorganised enterprises as a whole are from the FFIs. More than 41% of the capital investment is made by own fund. Borrowing from friends and relatives is another major source of capital investment. In case of the sample enterprises, borrowing from friends and relatives has 6% share in the overall capital investments expenditure. The indigenous money lenders’ and semi formal financial institutions’ share in overall capital investment was 2.4% and 2.9% respectively. In the manufacturing sector, 29% of the capital investment is financed by the entrepreneurs themselves and the share of FFIs is 59%. In the services sector, 45% of the capital investment is contributed by the entrepreneurs out of their pocket; while 46% comes from bank loans. Percentage share of own fund in capital investment is highest among the enterprises in the manufacture
of wooden furniture, fabricated metal products and internet cafes. Percentage share of borrowing from FFIs is relatively higher among the enterprises in manufacture of food products and beverages, land transport and food service activity. The indigenous money lenders have relatively higher share in the total amount of capital investment made by unorganised enterprises in the manufacture of wooden furniture, manufacture of textile and wearing apparels and trade and repairing of motor vehicles category.

In Guwahati, 35.3% of the capital investment is made by the entrepreneurs from their own fund; while 64.7% is borrowed from different sources. In Silchar, the situation is reverse; where the percentages share of own fund and borrowing from different sources are 66% and 34% respectively. In Guwahati, 52.9% of capital investment is borrowed from FFIs, while in Silchar only 24.7% is borrowed from the FFIs. The Semi Formal Financial Institutions (SFFIs) play a significant role in Guwahati, but those are absent in Silchar. The relative importance of money lenders is higher in Silchar; while that of friends and relatives is higher in Guwahati.

Here, it may be instructive to have an idea about the average amounts of loan taken by the enterprises from different sources (excluding those who have not taken any loan) during last five years. The average amount of loan per enterprise from FFIs is higher than that from any other sources. However, the variation is also highest among the enterprises regarding the size of loan from FFIs. Such variation is higher in Guwahati compared to that in Silchar. The maximum and minimum amounts of the loan from FFIs in Guwahati taken by unorganised enterprises is Rs.35,00,000 and Rs.50,000 respectively. In Silchar, the maximum and minimum sizes of the loan from FFIs are Rs. 10, 00,000 and Rs. 56,000 respectively. In Guwahati, the maximum and minimum sizes of the loans taken from SFFIs are Rs.305,000 and Rs.18,000 respectively. Both in Silchar and
Guwahati within the informal sources, the average size of the loan from friends and relatives is higher than that from indigenous money lenders. Moreover, the smallest amount of loan for capital investment is also taken from the friends and relatives. If this analysis is done including those who did not take any loan for capital investment during the last five years, it can be seen that the average size of the loans decline, the rest of the analysis remains more or less similar.

5.3: PATTERN OF FINANCING WORKING CAPITAL EXPENDITURE:

In addition to capital investment, enterprises also need loans for working capital expenditure. Working capital expenditure is that part of expenditure to run the day to day expenditure in the business; which includes expenditure on labourer, raw materials, taxes, TA, DA etc. Out of the total enterprises surveyed, 58 enterprises in Guwahati and 8 enterprises in Silchar took loans for working capital expenditure. Many enterprises in retail trading have balances with the suppliers of raw materials; which can also be regarded as one type of loan from the traders. Fourteen enterprises in Guwahati and five enterprises in Silchar are availing the Cash Credit (CC) facility. The percentage distribution of the enterprises surveyed according to their percentage of working capital expenditure made through borrowing can be explained with the help of Table: 5.1.

Table: 5.1: Percentage Distribution of Enterprises according to Percentage of their Working Capital Expenditure Made through Borrowing

<table>
<thead>
<tr>
<th>Source of Credit</th>
<th>No Loan (0%)</th>
<th>Up to 10%</th>
<th>10% to 20%</th>
<th>20% to 30%</th>
<th>30% or More</th>
</tr>
</thead>
<tbody>
<tr>
<td>All Sources</td>
<td>67.3</td>
<td>19.0</td>
<td>7.3</td>
<td>4.4</td>
<td>2.0</td>
</tr>
<tr>
<td>FFIs</td>
<td>89.3</td>
<td>3.4</td>
<td>3.4</td>
<td>2.4</td>
<td>1.5</td>
</tr>
</tbody>
</table>

Source: Field Survey, June-September, 2015

Table: 5.1, shows the percentage distribution of enterprises according to their percentage of working capital financed by borrowing. It can be seen that 67.3% of the enterprises took no loan to finance their day to day
expenditure in the business. Similarly, 89.3% of the enterprises took no loan from FFIs to finance their working capital expenditure. Thus, 22% of the enterprises took loans only from SFFIs and non institutional sources to finance their working capital expenditure. Only a few (1%) enterprises finance more than 50% of their working capital through borrowing and only one of the sample enterprises financed more than 50% of their day today expenditure through borrowing from FFIs. Here, queries arise regarding the pattern of financing working capital expenditure made by different categories of unorganised enterprises; which is explained with the help of figure: 5.2.

**Figure: 5.2: Pattern of Financing Working Capital Expenditure across Different Categories of Enterprises during Last One Year**

From figure: 5.2, it can be seen that around 97% of the capital investment made by the sample unorganised enterprises were financed by their own funds i.e. mainly return from their business. Around 2% of their day to day expenditure on business is financed by borrowings from FFIs and the rest is financed by non institutional and semi institutional sources. Manufacturing enterprises took relatively more credit from FFIs compared to service sector enterprises for this purpose. Enterprises in internet cafes took no loan to finance their working capital expenditure. SFFIs play relatively an important role in financing working capital expenditure of
enterprises in manufacture of textile and wearing apparels and trade and repairing of motor vehicles.

It is found that 96.6% of the working capital expenditure in Guwahati and that of 97.2% in Silchar was financed by the own funds of the entrepreneurs. None of the service sector enterprises in Silchar except those in retail trading took any loan for financing working capital expenditure. In Silchar, no enterprise took loan from informal money lenders and only one enterprise borrowed from friends and relatives for working capital expenditure. Rest of the picture is similar both in Guwahati and Silchar.

In case of working capital expenditure also, the average amount of loan per enterprise from the FFIs is higher compared to that from other sources; followed by that from the informal money lenders. Again the variation in the size of loan is also higher in case of informal money lenders.

5.4: BORROWING FOR OTHER THAN BUSINESS EXPENDITURE:

An entrepreneur may also borrow for purposes other than expenditure on their business. Sometimes, he needs credit to fill up the gap between expenditure and income receipt period. Similarly, he may take loan due to windfall losses in their business. Further, an entrepreneur may also take loans to invest in fixed asset and also for expenditure on consumer durables. Thus, all those loans taken by the entrepreneur under study were categorised into investment in fixed asset, expenditure on consumer durables and current consumption expenditure. Among the entrepreneurs the survey covered, 32.71% took loan at least once for other than expenditure on business. While 23.41% of the entrepreneurs took loan from FFIs; 5.85% borrowed from SFFIs. Only a few entrepreneurs took loans from indigenous money lenders and friends and relatives. Most of the loans originating from FFIs were either housing loan or car loans.
Thus, a larger percentage of those loans were either to create fixed asset (housing loan) or expenditure on consumer durables (bike or car).

**Figure: 5.3: Percentage Distribution of Loans taken by the Sample Entrepreneurs for Different Purposes other than Business during Last Five Years**

![Pie Chart: Percentage Distribution of Loans]

*Source: Field Survey, June-September, 2015*

**Figure: 5.4: Percentage Share of Different Agencies in the total Amount of Loan taken by Sample Entrepreneurs for Other than Expenditure on Business during Last Five Years**

![Bar Chart: Percentage Share of Different Agencies]

*Source: Field Survey, June-September, 2015*

To have a clear idea about the percentage distribution of loans taken for other than expenditure on business according to their utilisation Figure:
5.3 can be considered. This figure indicates that 42.03% of loans were taken for investment in fixed assets such as land purchase and house building. Maximum percentage of loan (i.e. 53.62%) was taken for expenditure on consumers’ durables and rest 4.35% of the loans were taken to meet the current consumption expenditure.

Sometimes an entrepreneur may borrow from different sources for the same purpose. Here, queries arise regarding the relative importance of different sources of credit for expenditure on other than business purposes. It can be seen (please refer to figure: 5.4) that more than 90% of the loan amount for other than expenditure on business was from FFIs. Entrepreneurs in fabricated metal product, food service activities and internet cafes took all the loans from FFIs. Entrepreneurs in the trade and repairing of motor vehicles took all the loans for expenditure on other than business either from SFFIs or indigenous money lenders. In Guwahati, out of the total amount of loans taken by the unorganised Entrepreneurs, 91.8% originated from FFIs and 5.2% was from SFFIs. The rest was from indigenous money lenders and friends and relatives. Entire amount of loan taken by the entrepreneurs in trade and repairing of motor vehicles in Guwahati was from SFFIs. In Silchar, SFFIs and friends and relatives have no share in the loans taken by the entrepreneurs for other than expenditure on business. The entire amount of loan taken by the entrepreneurs in trade and repairing of motor vehicles in Silchar was from money lenders. Entrepreneurs in rest of the categories in Silchar took loans only from FFIs.

Here, queries arise regarding the average size of the loan from different sources for expenditure on other than business by the entrepreneurs. It can be seen that the average amount of loan per unorganised enterprise (excluding those who have taken any loan for this purpose) from the FFIs taken for other than business purposes is also higher than that from any other sources. The variation in the average amount of loan is also higher
in case of FFIs. The highest and lowest amount of loan taken from the FFIs is Rs.25,00,000 and Rs.25,000 respectively. Similarly, the average amount of loan from the FFIs in Silchar is lower than that in Guwahati. In case of indigenous money lenders, the amount of the loans ranges between Rs.150,000 and Rs.29,000; while in case of friends and relatives, the amount of loan taken by the enterprise ranges between Rs.300,000 and Rs.2,000.

5.5: SUMMING UP:

The above discussion gives a clear picture of the pattern of financing of the sample urban unorganised enterprises. Borrowing from FFIs has been the main source of capital investment for the unorganised enterprises. However, own fund has also played a significant role in case of capital investment made by the sample unorganised enterprises. But, own fund has the maximum share in the total amount of working capital expenditure. The percentage share of borrowing from FFIs in working capital expenditure is very small. Thus, borrowing from FFIs has played an important role in case of capital investment; but not in case of working capital expenditure. The percentage share of non-institutional sources is very small both in case of capital investment and working capital expenditure. However, the SFFIs are playing a significant role in Guwahati in terms of financing expenditure of unorganised enterprises; but their presence is limited in Silchar. The informal money lenders have also played a relatively bigger role in Guwahati compared to that in Silchar. Larger percentage of loan taken by the entrepreneur’s household for other than expenditure on business, was either to create capital asset or for expenditure on consumer durables. Majority of such loans originated from FFIs.

Thus, the unorganised enterprises are found to be highly dependent on own fund for financing their business. But, starting a business investing entirely owned fund means the entire risk of the business is on that
particular entrepreneur. Moreover, scaling up the business primarily on own fund is a difficult proposition; specially for the unorganised enterprises. As a large percentage of them are engaged in such activity as they are unable to have a job in the organised sector. So, it can be assumed that if an entrepreneur makes the entire investment out of his pocket, he has limited access to credit. Here, queries arise regarding the factors limiting the unorganised entrepreneurs’ access to credit and other financial services. This analysis is done in the next chapter.